Public service pension contributions

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Author: Djuna Thurley

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In June 2010, the Conservative-Liberal Democrat Coalition Government established an Independent Public Service Pensions Commission, chaired by former Labour Secretary of State for Work and Pensions, Lord Hutton of Furness, to look at "the long-term affordability of public sector pensions, while protecting accrued rights". The Commission's interim report published in October 2010 concluded that the most effective way of making short-term savings was to increase employee contributions and that there was a "clear rationale" for doing this. It would be for the Government to decide the manner and level of any increases.

In response, the Government said it would implement increases to the level of employee contributions across public service schemes, except for the armed forces, equivalent to an average of 3.2 percentage points. The increases would phased-in: 40% of the increase would apply in 2012/13; 80% in 2013/14 and 100% in 2014/15. In order to protect the lower paid, the Government proposed that contributions should be tiered by earnings, with those earning less than £15,000 paying no extra and those earning less than £21,000 paying no more than 1.5% extra by 2014-15.

Scheme-by-scheme consultations on increases in employee contributions for 2012/13 - expected to save £1.2 billion - were launched at the end of July. The decisions on many of these reviews have now been announced. The Government is committed to securing further savings, rising to £2.8 billion in 2014-15, equivalent to a 3.2 pp increase. However, it is to review the impact of the 2012/13 contribution increases before taking final decisions on how future increases should be structured.

This note looks at the debate on the current proposals to increase contributions in public service schemes. The wider reforms are discussed in Library Standard Note SN 5678 *Public service pension reform - 2010 onwards*. Further detail on the reforms in individual schemes can be found in : SN 03260 *Firefighters' Pension Schemes*; SN 03224 *Civil Service Pension Scheme*; SN 01844 *Parliamentary Contributory Pension Fund*; SN0405 *Teachers' Pension Scheme*; SN 0700 *Police Pension Scheme,* SN 03280 *NHS Pension Scheme* and SN 5823 *Local Government Pension Scheme – 2010 onwards*.

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1 Background

Contribution rates vary widely across schemes. In most cases, both employers and employees contribute. One scheme - the armed forces scheme - is non-contributory for members, although pension benefits are taken into account when pay is assessed.[1] In others – the *classic* section of the civil service scheme and the scheme for the judiciary - members currently contribute towards the cost of survivors' benefits only.[2] Employee contributions fit into an overall remuneration package. So, low contribution rates may be matched by lower pay.[3]

The proportion of the cost of benefits met by employees varies across schemes. The Independent Public Service Pensions Commission noted that there has not been a standard formula for determining this:

> 1.7 The employee contribution rates – the percentage of salary that employees pay as an explicit contribution towards pension costs – have changed somewhat in recent years, but the general levels still reflect the historic legacy. For example, the civil service scheme only has standard contributions for members from 1972, initially only to pay for dependants' benefits. It retains rates of 1.5% or 3.5%. Employee rates of 5 per cent or 6 per cent for teachers, local government and the NHS date back to the first half of the 20th century. The average rates today are around 6.5 per cent.
>
> 1.8 There has not been a standard formula for determining the proportion of cost to be covered through employee contributions. However, some of the initial contribution

[1] AFPS 05, *Your Pension Scheme Explained*, (MMP/124, re-issued January 2007)
[2] Provision for judges to contribute to the cost of personal benefits was made in the *Pensions Act 2011*
[3] Independent Public Service Pensions Commission: Final Report, 10 March 2011, para 3.89

rates, such as for teachers and local government, were designed so that employees would meet half of the costs. At other times, such as when police and firefighters employee contributions were revised in the 1980s, the intention was the employee contributions should cover one third of the cost.[4]

Currently, employees either pay a low proportion of the total (as in the armed forces and civil service) or about one third of it (which is similar to the proportion paid by employees in the private sector):[5]

Table 3.G: Current contribution levels

Scheme	Employee contribution (%)	Employer contribution (%)	Proportion of total contributions paid by employees (%)
Teachers	6.4	14.1	31
NHS	5.5 - 8.5	14	26 - 38
Civil service	1.5 or 3.5	19[a]	6 - 17
Police - 1987 scheme	11	24.2	31
Police - 2006 scheme	9.5	24.2	28
Fire - 1992 scheme	11	26.5	29
Fire - 2006 scheme	8.5	14.2	37
Armed Forces - officers	0	37.3	0
Armed Forces - others	0	21.4	0
LGPS	5.5 - 7.5	14 - 25[b]	18 - 35
Average private sector (open DB)[c]	5.4	14.9	27
Average private sector (open DC)[c]	3.0	6.4	32

Source: IPSPC analysis of scheme data returns.

a) Average rate, employer contribution rates tiered by earnings.

b) Employer rates determined at individual fund valuations, and include contributions to fund past deficits, as do many of the employer contributions to the unfunded schemes.

c) Occupational pension schemes survey 2009.

The Commission commented that moving towards a more uniform structure of employee contribution rates would be complex:

Given the current range of rates and structures any transition to a more uniform structure for employee contribution rates will be complex. As mentioned previously, employee contribution rates fit into an overall remuneration package. In some schemes low rates may be matched by lower pay. At the extreme, the armed forces pay no contributions but an allowance for this is recognised when considering overall remuneration. Arguably, adjustments could be made to salaries to remove such effects across schemes without impacting on take-home pay to the employees, or to the cost of employment. However in order to do this, an assessment would be needed of how much of the difference in contribution rates between schemes is as a result of pay

[4] Ibid

[5] Independent Public Service Pensions Commission: Final Report, 10 March 2011; Table 3.G: Current contribution levels

> effects. The implications for total renumeration extend beyond the scope of this report and may require separate consideration.[6]

2 How contribution rates are set

Most of the large public service schemes (for example, those for teachers, civil servants, NHS, local government, police and firefighters) operate on a pay-as-you-go (PAYG) basis, meaning that there is no fund of assets which is invested and from which pension benefits are paid. Employer and employee contributions are paid to the sponsoring government department but these contributions are not invested. Instead, the sponsoring government department pays benefits to pensioner members, netting off the contributions received.[7]

Of the main public service schemes only the Local Government Pension Scheme (LGPS) is funded. This means that contributions are paid into a fund, which is invested, and from which pension benefits are paid. The LGPS is made up of a number of 89 funds in England and Wales administered and managed at local level, although the rules are set nationally by the Secretary of State.

Both funded and PAYG schemes are subject to regular actuarial valuations (generally, every 3-4 years). Part of the purpose of this is to assess the value today of pension benefits that will be paid in the future. Contributions (from employers and employees) are then set at an appropriate level to reflect that value.[8] For the PAYG schemes, the aim of this process is to make employers accountable for the pension costs accruing in respect of their employees and to ensure that such costs were recognised when taking decisions on staffing matters.[9] The LGPS, as a funded scheme, also has to ensure that it has sufficient assets to meet its liabilities over the longer-term. In the case of a funding deficit being identified, a recovery plan is drawn up, typically over a 20 year period. This is reflected in employer contribution rates.[10]

In the run up to the 2010 General Election, a number of commentators pointed out that the annual amount of contributions from employees and their employers was less than the estimated "current service cost" ("the amount that discounted pension scheme liabilities will increase over the year by reason of the additional year's service of active members of the pension scheme.")[11] BBC Economics Editor, Stephanie Flanders, for example, explained:

> No single number is going to decide that argument either way, but there is a number in the OBR report that might start that debate in the right place: that is their estimate of the "current service cost of public sector pensions", which they reckon was £26bn in 2007-8.
>
> In effect, that tells you how much the discounted value of all those pensions has gone up in a single year - how many new promises to pay money in the future the Treasury has taken on in a single year. (This is all horribly complicated, but think of it as the cost of buying a long-term annuity to pay off the 1/60th or 1/80th of salary that each

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[6] Independent Public Service Pensions Commission: Final Report, 10 March 2011, p79
[7] PPI, *an assessment of the Government's reforms to public sector pensions*, October 2008, p7
[8] HM Treasury, *Long-term public finance report 2009*, Box 6B
[9] Hewitt, *Principal Civil Service Pension Scheme – Review of the Accruing Superannuation Liability Charges (ASLCs) as at 31 March 2007,* 7 December 2007, Appendix E
[10] HC Deb, 13 May 2009, c819-20W;
[11] Office for Budget Responsibility, Pre-Budget forecast, June 2010. The Office for Budget Responsibility was created in 2010 to provide independent and authoritative analysis of the UK's public finances – see OBR website – what we do - http://budgetresponsibility.independent.gov.uk/about-the-obr/what-we-do/

member of these schemes has clocked up that year for his future pension - which can never be taken back.)

You can debate whether £26bn is the right number. You'll be relieved to hear that I'm not going to share that debate with you right now. But assume it's in the right ballpark. What the OBR is saying is that every year we, as taxpayers, are giving the five million or so people who work in the public sector rock-solid guarantees of future pension payments which, on the open market, would cost them at least £26bn a year.

In exchange for those promises, the individuals themselves are contributing £4.4bn, and their (government) employers are contributing £12.6bn - meaning a net subsidy by the Treasury of at least £10bn a year.[12]

The reason for the difference in the two figures[13] is that they are calculated on a different basis. The current service cost is calculated annually for each scheme and presented in the Resource Accounts. It is calculated according to IAS 19 (previously FRS 17) accounting standards and uses the AA corporate bond rate as the discount rate (to convert future cash flows to a single figure today).

Commentators objected that the different basis of these calculations means there was a significant annual subsidy "from the taxpayer to public sector employees (i.e. future pensioners) of which it appears that neither employers, employees, unions nor the taxpayer have any knowledge."[14] Following a recommendation of the Independent Public Service Pensions Commission, the Government conducted a review and has changed the discount rate used to set contributions (see section 4 below).

3 The Labour Government's reforms

The Labour Government introduced reforms to the schemes for teachers, NHS, local government and civil servants in 2007-08. The schemes for the uniformed services were reformed earlier, with new schemes for the armed forces, police, firefighters introduced in 2005 and 2006. The Independent Public Service Pensions Commission provided the following snapshot of the content of these reforms:

Ex.9 The previous Government recognised these issues and in 1997 started a series of significant reforms. These included:

- limited increases in pension age for groups such as the uniformed services, mostly for new entrants. In the civil service, NHS and teachers schemes existing members were allowed to keep a pension age of 60 if they wished, but new entrants have a pension age of 65 and pension ages lower than 65 will be phased out by 2020 in the Local Government Pension Scheme;
- sharing of risk arising from demographic change in the form of 'cap and share' rules. This spreads the cost of any future unexpected increases in contributions more equitably between employer and employees than previously, up to a cap after which any future increases would be borne by the members. Cap and share at present applies to the four biggest schemes – NHS, teachers, local government and civil service, although it has not yet

[12] Stephanie Flanders, *'(Some of) the truth about public sector pensions'*, 16 June 2010
[13] The figures for total annual contributions and current service cost
[14] Neil Record, *Sir Humphrey's Legacy – an update,* January 2008, page 12 ; See also, IFS Press Release, *The pension advantage of public sector workers*, 2 December 2009; CBI, *Clearing the pensions fog,* December 2008

affected employee contributions in any scheme and the Local Government Pensions Scheme does not yet have a cap set; and

- changed accrual rates for many of the reformed schemes, particularly for new entrants, but all except the civil service are still based on final salary. The change to a career average structure in the civil service scheme was not primarily undertaken as a cost saving measure, but as a response to the changing nature of the workforce.[15]

3.1 Changes to contribution rates

As explained above, the reforms introduced by the Labour Government included changes to employee contribution rates.

In the case of the Teachers' Pension Scheme, for example, employee contribution rates increased from 6% to 6.4% with effect from January 2007.[16] Tiered contribution rates, according to pay, were introduced as part of reforms to the NHS and Local Government Schemes in April 2008:

- In the NHS Pension Scheme, employees now contribute between 5% and 8.5%. This compares to contribution rates prior to reform of 6% or 5% (manual staff).[17]

- In the Local Government Pension Scheme, employees now contribute between 5.5% and 7.5% of pay.[18] Before this, there was a standard employee contribution rate of 6%, except for certain members with "lower rate rights", who contributed at 5%.[19]

In the schemes for the police and firefighters, on the other hand, members of post-reform schemes, pay lower contribution rates than members of the existing schemes.[20] This reflected the fact that the new schemes cost less both for employee and employer due to increases in the pension age and changes in accrual rates.[21]

In the Principal Civil Service Pension Scheme, members of the *classic* scheme (closed to new entrants from October 2002) pay 1.5% of pay. When *premium* was introduced in 2002 with improved survivors' benefits, a higher rate of employee contributions was set (3.5%) in order that the reforms would be cost-neutral.[22] Members of the *nuvos* scheme introduced in 2007 also contribute 3.5% of pay.

3.2 'Cap and share'

Mechanisms to limit the liability of the taxpayer to unanticipated future rises in cost ("cap and share" arrangements) were introduced as part of reforms to the schemes for NHS, local

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[15] Independent Public Service Pensions Commission: Interim Report, 7 October 2010

[16] Details of contributions to the TPS from 2002-3 to 2006-07 can be found in HC Deb, 20 October 2008, c84W

[17] *NHS Pension Scheme Regulations 1995 (SI 1995/300),* Section D1

[18] *Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (SI 2007 No, 1166)*, reg 3

[19] *Local Government Pension Scheme Regulations 1997*, regulation 12.

[20] 9.5% for members of the New Police Pension Scheme 1987 compared to 11% for members of the Police Pension Scheme 1992; and 8.5% for members of the New Firefighters Pension Scheme 2006 compared to 11% for members of the Firefighters Pension Scheme

[21] Explanatory memorandum to the Firefighters' Pension Scheme (England) Order 2006 (SI 2006/3432); Explanatory Memorandum to the *Police Pensions (Amendment)Regulations 2008* (SI 2008/1887), para 7.8

[22] HC Deb, 22 July 2002, cc728-30WS

government, teachers and civil servants in 2007/08. HM Treasury explained what the policy was intended to achieve:

> The cap and share policy is designed to ensure that the cost pressures associated with the rising cost of providing pension scheme benefits (such as improving longevity) are shared between employers and employees up to an agreed employer contribution cap, beyond which all further increases will be the responsibility of employees. This sets a maximum limit to employer contributions thus protecting the public finances and taxpayer. The costs will be assessed through the periodic scheme valuations that take place every 3 or 4 years.[23]

The cap and share arrangements were expected to take effect in 2012/13.[24] In many cases, the employer contribution was already at or near the cap, implying that any increase in costs would largely be met by employees.[25] The Independent Public Service Pensions Commission commented that the policy intention appeared to be to "keep the levels of employer cost no higher than those reached around 2004 and 2005."[26]

The Labour Government expected the policy to save "an estimated £1 billion a year from 2012-13, and at least twice this amount over the long-term."[27]

In December 2010, the National Audit Office published its assessment of changes made to Teachers', NHS and civil service schemes in 2007-08. The main changes aimed at reducing and better managing taxpayer costs were: increased contribution rates for NHS staff and teachers; an increase in the normal pension age from 60 to 65 for most new staff; and a cost sharing and capping mechanism. The NAO concluded that:

> As a result of the changes, which are on course to deliver substantial savings, long-term costs are projected to stabilise around their current levels as a proportion of GDP. The changes are also set to manage one of the most significant risks to those costs, by transferring from taxpayers to employees additional costs arising if pensioners live longer than is currently projected.[28]

It expected the changes to reduce annual costs to the taxpayer by 14 per cent in 2059-60, compared to what they would have been without the changes.[29] If cost sharing and capping worked as expected, it would account for 49 per cent of the savings in 2059-60.The NAO commented that cap and share was "designed primarily to prevent costs from changing unexpectedly rather than to reduce them." The size and timing of any savings was subject to risk and uncertainty for a number of reasons:

> – The mechanism gives Ministers discretion in deciding precisely how to implement cost sharing and capping, so it may not have the impact projected in this report.
>
> – Savings will be smaller if certain cost pressures turn out to be lower than expected, for example if future increases in pensioners' life spans are less than currently projected. Overall costs will, however, stay broadly the same, in line with the

[23] HM Treasury, Long-term public finance report: an analysis of fiscal sustainability, December 2009, Box 6.A
[24] NAO, The impact of the 2007-08 changes to public service pensions, HC 662, Session 2010-2011, para 2.2
[25] This is discussed in more detail in Library Standard Note 5252, Public service pension schemes – cost capping and sharing (section 3)
[26] Independent Public Service Pensions Commission: Interim Report, 7 October 2010, p45-6
[27] HM Treasury, Pre Budget Report 2009, para 6.51
[28] NAO, The impact of the 2007-08 changes to public service pensions, HC 662, Session 2010-2011, para 2.1
[29] Ibid

design of the mechanism. The reverse applies if cost pressures turn out to be higher than expected.

– The timing of savings depends on the completion of actuarial valuations. Our projections assume that cost sharing and capping will be implemented in 2012-13, as the Treasury currently expects. The delay from previous expectations is partly because the Treasury has suspended actuarial valuations while it reviews what discount rate to use in them.[30]

In its interim report, the Independent Public Service Pensions Commission noted that “cap and share” was as yet an “untried system” and had a number of limitations:

> [...] cap and share on its own will not deliver the type of wide-ranging structural reforms that are needed or significant reductions in current costs for taxpayers. It would instead be necessary to apply a more coherent overall policy framework when determining future pension provision and how levels of employer cost and risk are assessed, managed and taken into account in overall remuneration.[31]

These reforms are discussed in more detail in Library Standard Note SN 5252 *Public service pension schemes – cost capping and cost sharing.*

4 The approach of the current Government

4.1 Independent Public Service Pensions Commission

In Budget 2010, the current Government announced the establishment of the Independent Public Service Pensions Commission, to be chaired by former Labour Work and Pensions Secretary of State, Lord Hutton of Furness. The Commission would:

> ...undertake a fundamental, structural review of public service pension provision by Budget 2011 and consider the case for short-term savings in the Spending Review period, by September 2010.[32]

In its interim report, the Commission concluded that an increase in member contribution rates was the most effective way of making short-term savings. Furthermore, there was a case for doing so. In his foreword to the report, Lord Hutton said:

> I consider there is [....] a strong case for looking at some increase in pension contributions for public service employees, to better meet the real costs of providing these pensions, the value of which has risen in recent years with most of these extra costs falling to taxpayers.[33]

The manner and level of any increases in contributions would be for the Government to decide. The Commission recommended that this should be done with a view to preventing a significant increase in opt-outs:

> [...] any increases should be managed so as to protect the low paid and, if possible, increases in contributions should be staged and need to be considered with a view to

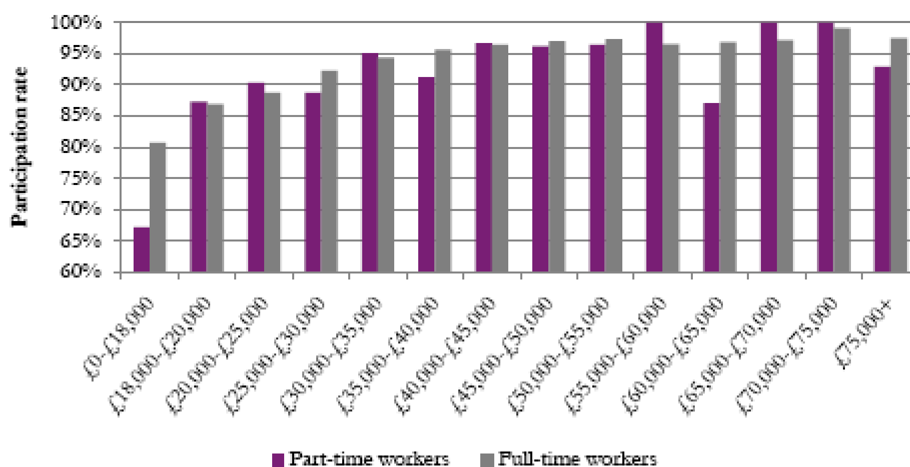
[30] Ibid
[31] Independent Public Service Pensions Commission: Interim Report, 7 October 2010, page 47
[32] HM Treasury, Budget 2010, HC 61, June 2010
[33] Ibid, foreword

preventing a significant increase in opt out rates. The Commission does not recommend introducing contribution rates for the armed forces at this time.[34]

The introduction of tiered contribution rates could mitigate the risk of increased opt-outs by low-earners:

3.86 Furthermore, Chart 3H participation rates vary across all public service pension schemes by salary and by employment status. The general trend shows increasing participation with increasing salary, flattening out at higher earnings levels. The opt-out rate for those earning under £18,000 is almost 20 per cent, increasing to over 30 per cent for part-time workers.

Chart 3.H: Participation rate by earnings



Source: IPSPC analysis of data from the Annual Survey of Household Earnings.

3.87 There is therefore a case for different treatment of higher and lower earners to encourage greater participation amongst low-paid and part-time workers. It could be argued that contributions should be weighted so that those who earn more pay the most. Lower contribution rates for the lower paid encourages participation in pension schemes, contributing to higher provision in retirement and less reliance on state benefits[35]

The Commission suggested that the Government might wish to take account of "effective employee benefit rates" in deciding how contributions should increase. This is a measure enables the generosity of different schemes to be compared:

This concept tries to reflect the average value of the benefits of the pension to an individual as a proportion of their salary by taking account of the features of the scheme such as the accrual rate, the Normal Pension Age and any other benefits offered by the scheme. These rates show the average additional value of the pension to the individual. Since they are averages, actual rates will vary significantly across individuals, depending on factors such as age, scheme rules etc. Employee

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[34] Independent Public Service Pensions Commission: Interim Report, 7 October 2010
[35] Independent Public Service Pensions Commission: Final Report, 10 March 2011, ibid, p78-9

> contributions are deducted so that the effective benefit rates only include the part of the benefits funded by the employer.[36]

Average effective benefit rates varied substantially between schemes. For members of the uniformed services, they are relatively high, due to lower retirement ages and faster accrual rates:

> The reformed NHS, principal civil service and teachers schemes have average effective benefit rates of approximately 17 per cent of salary, close to the level of an average private sector defined benefit scheme (although as show in Chapter 1 few of these remain open). The armed forces scheme is worth 32 per cent of salary, the police close to 23 per cent and the fire service around 20 per cent.
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> 5.20 Many of these differences are due to lower retirement ages and faster accrual in the uniformed services. Since the rates are net of employer contributions, the level of employee contributions is also important and the higher rate for the armed forces scheme in part reflects the fact that this scheme is non-contributory.[37]

The schemes for uniformed services have traditionally had relatively low normal pension ages, justified by the need for a recognised physical capacity to do the job.[38]

The Commission pointed out that many of the differences in benefit levels had arisen because of historic negotiations and developments:

> [...] 5.23 However, many of the differences in the level of benefits delivered by schemes have arisen because of historic negotiations and developments, in particular on the extent to which pensions have been allowed for when setting pay. For example, when setting military pay rates, the Armed Forces Pay Review Body includes the value of the value of the military pension when considering pay compatibility with civilians.[39]

The Commission also recommended a review of the discount rate used to set contributions. It questioned whether the discount rate then in use (a fixed level of 3.5% in excess of inflation, in line with the Social Time Preference Rate[40]) was appropriate:

> 8.6 A further complication is the extent to which the cost of pensions promises are being properly accounted for. Pension costs are split between employers and employees after the total contributions required have been calculated. This calculation involves using the discount rate that was discussed in Chapter 4. If the discount rate currently in use by schemes for making calculations about the size of contributions required is too high, then costs will be underestimated.
>
> 8.7 The Commission is asking the Government to review this rate. If they reach the conclusion that the rate is too high then total contributions to schemes will need to rise. The Commission estimates that reducing the discount rate by half a per cent, for example, could increase the total contribution rate by nearly three per cent of pensionable payroll. There is then the issue of how this increase is split between employers and employees.

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[36] Ibid, Box 5.B
[37] Ibid
[38] See, for example, DWP, HM Treasury, Inland Revenue, *Simplicity, security and choice: working and saving for retirement*, December 2002, Cm 5677, para 66
[39] Ibid
[40] For an explanation, see HM Treasury, Green Book, Annex 6 and Independent Public Service Pensions Commission: Interim Report, 7 October 2010, Box 4E

> 8.8 Because most of the increased costs to date, driven by longevity improvements in particular, have been financed by employers in the form of increased contributions, there is an argument that employees should pay a greater share of the extra cost, as they are the principal beneficiaries of this unexpected increase in the cost of their pension.[41]

4.2 The Government's response

Overview

In response to the Commission's interim report, the Government said it intended to implement 'progressive changes' to employee contributions, phased-in from April 2012:

> The Government will implement progressive changes to the level of employee contributions equivalent to an average of three percentage points, to be phased in from April 2012. The armed forces will be exempt from this increase. Full details, including consideration of Lord Hutton's recommendation to phase in the increase and provide protection for the low paid will be announced at Budget 2011.[42]

When the armed forces are excluded, the increase across the other schemes is 3.2 percentage points.[43] This was expected to lead to savings of £2.8 billion a year by 2014-15. This figure subsumes the £1 billion of savings already expected through cap and share mechanisms. It does not include any savings from the Local Government Pension Scheme (LGPS). The share of the total was distributed across other schemes proportionately to the size of each scheme's paybill.[44]

Also, as recommended by the Commission, the Government launched a *consultation on the discount rate used to set unfunded pension contributions* in December 2010. A summary of responses to the consultation was published in April 2011. In the 2011 Budget, the Chancellor announced that the discount rate would be reduced:

> Today we publish the result of our consultation on the discount rate, which shows that a more appropriate rate would be inflation plus GDP growth. This reinforces our case for increasing the employee contributions by an average of 3%. Indeed, the new discount rate could be used to justify further contribution rises. As part of the wider reforms, I am not proposing to ask for more than the 3% average.[45]

In July 2011, the Chief Secretary to the Treasury announced scheme-level discussions on contribution increases. He also outlined the Government's plans how the increases should be phased in: so that 40% of the increase would apply in 2012/13; 80% in 2013/14 and 100% in 2014/15. As regards protection for the lower paid, he proposed that:

- Those earning less than £15,000 (full-time equivalent rate) would pay nothing extra;

- Those earning up to £21,000 (full-time equivalent will pay no more than 0.6% of pay extra in 2012-13 (and no more than 1.5% of pay extra in total by 2014-15);

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[41] Ibid

[42] HM Treasury, Spending Review – policy costings, October 2010. HM Treasury, Public Service Pensions: good pensions that last, Cm 6214, November 2011, para 1.7

[43] HC Deb, 14 July 2011, c486W

[44] HL Deb, 7 February 2011, cWA31; Independent Public Service Pensions Commission: final report, March 2011, para 1.16; HC Deb, 1 March 2011, c437-8

[45] HC Deb, 23 March 2011, c961

- Higher earners would pay extra, but not more than 2.4% of pay in 2012-12 (and no more than 6% of pay extra in total by 2014-15).[46]

The Government recognised that the local government scheme was in a different position and would discuss whether there are alternative ways to deliver some or all of the savings.[47] Discussions are ongoing on a one step reform process for the LGPS, with the potential for no contribution increases, provided the overall financial constraints set by Government were met. Decisions on contribution rates for 2012-13 have now been announced for most of the other main public service schemes (see below).

On 20 December, he said the impact of the 2012/13 increases would be reviewed before final decisions were taken on how future increases would be delivered:

> The Government is not proposing any further increase in the total employee scheme contribution rates in addition to the 3.2 percentage points increase in contributions already announced. The Government will review the impact of next year's increases, including on opt-outs and equality, before taking final decisions on how future increases will be delivered. Interested parties will have the opportunity to provide evidence and views to the Government.[48]

In March 2012, the Government announced details of Proposed Final Agreements for the design of new schemes for the NHS, teachers, civil service and firefighters to be introduced in 2015. These included proposals for average contribution rates in the new scheme. Further details are provided below.

Implementation plans by scheme

Civil service

Proposals for increases in member contribution rates for 2012/13 were put forward by the Cabinet Office in July 2011.[49] The table below shows the contribution rates for members of *classic, premium, nuvos* and *classic plus* in 2011/12 and 2012/13:

[46] HC Deb, 19 July 2011, c91-4; Cabinet Office, Principal Civil Service Pension Scheme – Consultation on proposed increases to employee contribution rates effective from April 2012, July 2012
[47] HC Deb, 19 July 2011, c91-4 WS
[48] HM Treasury press release, Government announces Heads of Agreement on public service pension reform, 20 December 2011
[49] Principal Civil Service Pension Scheme – Consultation on proposed increases to employee contribution rates effective from April 2012

Pensionable pay (FTE)	Contribution rate 2011/12 - *classic* (%)	Proposed additional rate for 2012/13 (%)	Contribution rate 2012/13 - *classic* (%)	Contribution rate 2011/12 - *premium, nuvos and classic plus* (%)	Contributi on rate 2012/13 - *premium, nuvos and classic plus* (%)
> £15,000	1.5	Nil	1.5	3.5	3.5
£15,001 - £21,000	1.5	0.6	2.1	3.5	4.1
£21,001 - £30,000	1.5	1.2	2.7	3.5	4.7
£30,001 - £50,000	1.5	1.6	3.1	3.5	5.1
£50,001 - £60,000	1.5	2.0	3.5	3.5	5.5
Over 60,000	1.5	2.4	3.9	3.5	5.9

The Cabinet Office published its response to the consultation in December 2011. It concluded that the "case for change still stands" and that the proposals set out in July would be implemented.[50] It said there were "no plans to change the rate of employer contributions (currently 18.9%) "at this time."[51]

The tiering structure of member contribution rates for 2013-14 and 2014-15 is to be reviewed in the light of experience: [52]

Contribution Increases for 2013-14 and 2014-15

17. Contribution structures in 2013-14 and 2014-15, before the new scheme is introduced, will be discussed by Cabinet Office and unions in the light of experience of opt-outs, other member behaviour and changing circumstances, and will reflect the Government's and unions' shared priorities for those structures to:

- include protections for the low paid,
- take account of the tax regime applicable at that time,
- minimise the risk of opt-outs from the scheme across the whole membership; and
- ensure that the scheme remains sustainable, a valuable part remuneration, and affordable to all members.

18. Relevant data and information will be collated to inform a Government review of tiering structures in advance of Cabinet Office consulting with Trades Unions and other interested parties on the contribution structures for 2013-14 and 2014-15. Information will include data on opt-out following the 2012-13 increases and also an assessment of members' expected behaviour in response to further increases in contribution rates.

[50] Cabinet Office, Principal Civil Service Pension Scheme – Consultation on proposed increases to employee contribution rates effective from April 2012 – Government response, 15 December 2011; See also Q&A for pension contribution increases.
[51] Cabinet Office – Q and A for pension contribution increases
[52] Cabinet Office, Civil Service Pension Scheme – Proposed Final Agreement, 9 March 2012

> The tiering structure for 2013-14 and 2014-15 would be subject to the requirement to meet the Government"s spending review commitments in 2013-14 and 2014-15 across unfunded public service pension schemes.

In March 2012, the Cabinet Office published its Proposed Final Agreement for a new Principal Civil Service Pension Scheme to be introduced in 2015. It was proposed that this new scheme would have an average member contribution rate of 5.6%:

> **Contributions from April 2015 onwards**
>
> 19. The contribution structure from April 2015 onwards will be considered by the Cabinet Office and unions following a further review. The review will cover the key priorities set out above, consider the final contributions structures for 2013-14 and 2014-15, and ensure the structure delivers the average member contribution rate of 5.6% based on current forecasts. It will also take account of the differences in design between the pre 2015 and post 2015 schemes, having regard to such factors as the career average structure of the schemes post-2015 but with a retention of final salary linkage for accrued service, and the 10 year protection.
>
> 20. The following indicative tiering structure is subject to the reviews and consultations described above, but based on current assumptions would meet the requirements set out:

Annual pensionable salary (full time equivalent basis)	Contribution rate (% of pensionable pay) before tax relief
Up to and including £21,000	4.6%
£21,001 - £45,000	5.45%
£45,001 - £149,000	7.35%
£150,000 and above	9.0%

NHS

In July 2011, the Department of Health (DoH) published its *Consultation on proposed increases to employee contribution rates effective from April 2012*. In December, it issued a revised proposal. The threshold of earnings below which there would be no increase in contributions would be raised from £15,000 to £26,557. To pay for this, there would be a "small increase in the contribution paid by members within the £26,558 to £48,982 and the £48,983 to £69,931 bands." It had decided that the distribution of increases should take into account the effect of tax relief:

> 5.5 NHS Employers and several other respondents argue that there is a strong case for reconsidering the distribution of increases for 2012-13 (and for future increases in 2013-14 and 2014-15) on a net rather than a gross basis. This would facilitate, over the three year period to 2014-15, the Government objective to apply increases progressively - basing these on the actual burden that falls on members. We therefore agree with this conclusion.[53]

[53] DoH, NHS Pension Scheme. Consultation on proposed increase to employee contribution rates effective from April 2012, Government response, 8 December 2012

The following table shows how contribution rates are to increase in 2012/13:[54]

Full-time 2010/11 pay	2010/11 contribution	2012/13 contribution	Contribution increase (percentage points)
Up to £15,000	5%	5%	0
£15,001 to £21,175	5%	5%	0
£21,176 to £26,557	6.5%	6.5%	0
£26,558 to £48,982	6.5%	8%	1.5
£48,983 to £69,931	6.5%	8.9%	2.4
£69,932 to £110,273	7.5%	9.9%	2.4
Over £110,273	8.5%	10.9%	2.4

The Government has determined that the average member contributions will be increased from 6.6% in 2011/12 in stages to 9.8% in 2014/15. The tiering structures for 2013-14 and 2014-15 are to be reviewed in the light of experience:

> 10. Tiering structures in 2013-14 and 2014-15, before the new scheme is introduced, will be discussed by the Department, NHS Employers and unions in the light of experience of opt-outs, other member behaviour and changing circumstances, and will reflect the Government's and unions' shared priorities for those structures to:
>
> - include protections for the low paid,
> - minimise the risk of opt-outs from the scheme across the whole membership; and
> - ensure that the scheme remains sustainable, a valuable part remuneration, and affordable to all members.
>
> 11. Final contributions structures across all unfunded public service pension schemes for 2013-14 and 2014-15 will meet the Government's spending review commitment.[55]

The employer contribution is to remain at 14%, although this may change in future:

> **Will the level of employer contribution change?**
>
> Under these proposals the employer contribution would remain the same – 14%. However, the Government is committed to introducing long-term reforms of public service pension arrangements that would take effect from 2015 onwards. The level of employer contribution may therefore be subject to change in the future.[56]

In March 2012, the DoH published its Proposed Final Agreement on the scheme design for a new NHS Pension Scheme for England and Wales to be introduced from 2015. This included a proposal for "member contributions on a tiered basis to produce a total yield of 9.8% of total pensionable pay in the Scheme", subject to detailed arrangements for determining future contribution structures:

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[54] Ibid, p17
[55] DoH Proposed Final Agreement – Reforming the NHS Pension Scheme for England and Wales, February 2012
[56] DoH – additional Q&A on contribution increases

12. The tiering structure in the new scheme will be considered by the Department, NHS Employers and unions following a further review. The review will cover the key priorities set out above, consider the final contributions structures for 2013-14 and 2014-15, and ensure the structure delivers the required yield of 9.8% of total pensionable pay in the Scheme based on current forecasts. It will take account of the issues set out in paragraph 9 and also consider the differences in design between the pre 2015 and post 2015 schemes, having regard to such factors as the career average structure of the schemes post-2015 but with retention of final salary linkage for accrued service, and the 10 year protection.[57]

Annex E to the document sets out an indicative contribution rate structure in 2014/15, after implementation of an increase in average member contribution rates of 3.2 percentage points to 9.8%.

Teachers

In July 2011, the Department for Education published its Consultation on Proposed Increases to Contributions for Members of the Teachers' Pension Scheme. In December, it announced that it had decided to implement the increases proposed in July.[58] The member contribution rates to be implemented from April 2012 are shown in the table below:[59]

Lower Salary	Higher Salary	Contribution Rate in 2012-13	Increase (against 6.4%)	Membership	% of member-ship
	14,999	6.4%	0%	1,400	0.2%
15,000	25,999	7.0%	0.6%	116,000	17.1%
26,000	31,999	7.3%	0.9%	117,000	17.2%
32,000	39,999	7.6%	1.2%	271,000	39.6%
40,000	74,999	8.0%	1.6%	172,000	25.2%
75,000	111,999	8.4%	2.0%	4,000	0.6%
112,000		8.8%	2.4%	600	0.1%

The employer contribution rate (currently 14.1%) is to remain unchanged in 2012-13.[60]

The tiering structures for contribution increases in 2013-14 and 2014-15 are to be considered in the light of experience:

Contribution increases for 2013-14 and 2014-15

Employee contributions will be increased from 1st April 2012 to reflect the outcome of the recent consultation by the Department for Education. The Department has proposed a number of potential tiering structures for the following two years. Any such tiering structures will be discussed by the Department and unions in the light of experience of opt-outs, other member behaviour and changing circumstances.

[57] Ibid

[58] DfE, Consultation on proposed increases to contributions for Members of the Teachers' Pension Scheme – consultation response, December 2011

[59] DfE, Teachers' Pension Scheme – Proposed Final Agreement, March 2012

[60] DfE, Consultation on proposed increases to contributions for members of the Teachers' Pension Scheme, July 2012

Relevant data and information will be collated to inform a Government review of tiering structures in advance of the Department consulting on contribution increases for 2013-14 onwards. Information will include data on opt-out and also an assessment of members' expected behaviour in response to further increases in contribution rates. This work will be taken forward within the context of the Government's wider consideration of tiering structures across public service pension schemes. Consideration of tiering structures for 2013-14 and 2014-15 will reflect the Government's and unions' shared priorities for those structures that they should:

include protections for the low paid,

minimise the risk of opt-outs from the scheme across the whole membership, including for example, newly-qualified teachers and lecturers and part time workers; and

ensure that the scheme remains sustainable, a valuable part of teachers' and lecturers' remuneration, and affordable to all members.

Consideration will also be given to the case for and against a progressive tiering structure.

Both the review and the consultation will be informed by available information on experience across all relevant public service schemes. The tiering structure for 2013-14 and 2014-15 would be subject to:

- the review of opt-out referred to above, that unions and other interested parties will feed into; and
- the requirement to meet the Government's spending review commitments in 2013-14 and 2014-15 across unfunded public service pension schemes.[61]

In December 2012, the Department for Education published its Proposed Final Agreement on the scheme design for a new Teachers Pension Scheme to be introduced from 2015. This included a proposal for "member contributions on a tiered basis to produce a total yield of 9.6% of total pensionable pay in the Scheme", subject to detailed arrangements for determining future contribution structures:

Contribution Rates for 2015 onwards

The Department and unions will carry out a separate and further review to determine the contribution rate structure to apply from 1st April 2015. The scope of the review will cover the key areas for consideration set out above (i.e. for the 2013-14 and 2014-15 tiers) and will ensure that the structure delivers the average member contribution of 9.6%. It will also take account of the differences in design between the pre 2015 and post 2015 schemes, having regard to such factors as the retention of final salary linkage for accrued service and the 10 year protection.

The review will reflect member behaviour, especially in respect of opt-out since the introduction of tiered contributions and will build upon the earlier review. The Department will undertake an equality impact assessment, which will inform consultation on the contributions from 2015 onwards.[62]

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[61] DfE, Teachers' Pension Scheme – Proposed Final Agreement, March 2012
[62] Ibid

Local Government

Responding to the proposed contributions increase, the Local Government Group[63] argued that the Local Government Pension Scheme (LGPS) should be treated differently because it operates on a funded basis. It was concerned, for example, that if the proposed increase in contributions led to significant numbers of employees opting out, this could have "a serious and detrimental impact on the Scheme's future sustainability and viability". It could also mean:

> LGPS Funds would become more mature leading to a move away from equities into bonds. This could distort the bond market and a move out of UK equities (in which the LGPS Funds have significant holdings) could have an impact on the UK investment sector (FTSE).[64]

The Government accepted that the LGPS was in a different position and agreed to "discuss whether there are alternative ways to deliver some or all of the savings."[65] The CLG set out initial proposals for short terms savings, involving a combination of contribution increases and changes to accrual rates.[66]

On 20 December 2011, the Secretary of State for Communities and Local Government announced agreement on the principles that would govern the design of a new local government scheme for local government workers. The objective would be to roll the requirements for short-term savings and long-term reform into a 'one step' process, with the potential for no contribution increases, provided the overall financial constraints set by Government were met:

> The core parameters of the agreed new scheme design are set out below:
>
> a. a single solution to both the short and long term issues by the early introduction of the new scheme in April 2014, with regulations in place by April 2013;
>
> b. the single solution to be built on the basis of career average earnings;
>
> c. can include zero increases in employee contributions for all, or the vast majority of members, provided that overall financial constraints set by the Government are met;
>
> d. some elements of choice to encourage retention of existing membership and encourage new membership; and
>
> e. flexible retirement age built around the scheme's normal retirement age equal to the state pension age or age 65, whichever is later, and applies both to active members and deferred members (new scheme service only). If a member's state pension age rises, then normal pension age will do so too for all post 2015 service.[67]

On 21 December, local government unions and employers issued a joint statement to the effect that the agreement reached provided the "best possible route to a simple and sustainable scheme which is affordable for members and employers".[68]

Firefighters

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[63] Formerly known as Local Government Employers
[64] Letter to Chancellor from Local Government Group, 16 February 2011
[65] HC Deb, 19 July 2011, c91-4 WS
[66] Letter to Local Government Pension interests in England and Wales, 7 October 2011
[67] HC Deb, 20 December 2011, c153WS
[68] GMB press release, 'Local Government deal on pensions removes the threat of huge contribution rises which would have led to mass opt outs and jeopardised the LGPS funds, says GMB', Thursday 22 December 2011

A consultation document on increases in member contribution rates for the Firefighters Pension Scheme in 2012-13 was published in July 2011.[69]

A summary of responses to the consultation was published on 29 March 2012. In response to consultation responses, the Government had decided to proceed with a smaller increase in April 2012 than originally proposed:

> Ministers have concluded that the case for change still stands but that it is appropriate, in the specific case of the firefighters' pension scheme and in consideration of the responses to the statutory consultation exercise, to proceed with an altered contribution rate increase from April 2012.[70]

The contribution rates for two firefighters' schemes in 2011/12 and 2012/13 are in the table below:

Firefighters' Pension Scheme 1992

Pensionable pay band	Contribution rate 2011/12	Increase in 2012-13 (%)	Contribution rate 2012-13 (%)
> £15,000	11.0	0.0	11.0
£15,001 - £30,000	11.0	0.6	11.6
£30,001 - £40,000	11.0	0.7	11.7
£40,001 - £50,000	11.0	0.8	11.8
£50,001 - £60,000	11.0	0.9	11.9
£60,001 - £100,000	11.0	1.2	12.2
£100,001 - £120,000	11.0	1.5	12.5
More than £120,000	11.0	2.0	13.0

[69] CLG, Firefighters' Pension Scheme (1992) and New Firefighters' Pension Scheme (2006) Proposed increases to employee contributions rates, effective from 1 April 2012 - consultation
[70]

New Firefighters' Pension Scheme 2006

Pensionable pay band	Contribution rate 2011/12	Increase in 2012-13 (%)	Contribution rate 2012-13 (%)
> £15,000	8.5	0.0	8.5
£15,001 - £30,000	8.5	0.3	8.8
£30,001 - £40,000	8.5	0.4	8.9
£40,001 - £50,000	8.5	0.5	9.0
£50,001 - £60,000	8.5	0.6	9.1
£60,001 - £100,000	8.5	0.8	9.3
£100,001 - £120,000	8.5	1.0	9.5
More than £120,000	8.5	1.2	9.7

For the new scheme to be introduced from April 2015, the "heads of agreement" proposed an average member contribution rate of 13.2%:

> Average member contributions of 13.2% from April 2015, with some protection for new entrants. However, as announced by the Chief Secretary to the Treasury on 20 December, the Government will review the impact of the proposed 2012-13 contribution changes, including the effect of membership opt-outs, before taking final decisions on how future increases will be delivered in 2013-14 and 2014-15, and in the new scheme.[71]

The structure of employee contribution rates in 2015-16 "has yet to be finalised but may be structured so that lower paid staff pay lower contributions."[72]

Police

A consultation document on increases in member contribution rates for the Police Pension Scheme in 2012-13 was published in July 2011.[73] On 30 January 2011, Home Secretary, Theresa May announced that member contribution rates would increase in 2012/13 in line with the proposal put to the Police Negotiating Board (PNB) in July. The PNB would be asked to consider the proposed increases for 2013/14 and 2014/15.[74]

The contribution rates for 2011/12 and 2012/13 are in the table below:[75]

[71] Department for Communities and Local Government, Firefighters' Pension Scheme: Heads of Agreement, February 2012

[72] Department for Communities and Local Government, Firefighters' Pension Scheme reforms – FAQs, February 2012

[73] Letter from Home Secretary to Staff Side of Police Negotiating Board, 29 July 2011

[74] HC Deb, 30 January 2012, c33WS

[75] Home Office circular – 004/12 – Increased police officer pension contributions; The increases for 2012 were implemented by the *Police Pensions (Amendment) Regulations 2012* (SI 2012 No. 640)

	Contribution rates 2011/12	Increase in 2012-13	Contribution rates 2012/13
Tier 1 - PPS 1987	n/a	n/a	n/a
Tier 1 - NPPS 2006	9.5%	0.60%	10.10%
Tier 2 - PPS 1987	11.0%	1.25%	12.25%
Tier 2 - NPPS 2006	9.5%	1.00%	10.5%
Tier 3 - PPS 1987	11.0%	1.50%	12.5%
Tier 3 - NPPS 2006	9.5%	1.25%	10.75%

The Police Federation wrote to the Home Secretary on 10 April to express concern about the increases for 2012/13 and highlighting the fact that the proposed increases for firefighters had been altered following consultation:

> Staff Side was extremely concerned about the proposed increases for many reasons, including:
>
> - the fact they bore no relation to the value of providing scheme benefits;
> - members of the police schemes already pay the highest contribution rates in the public sector and would therefore bear the brunt of the increases;
> - the costs of police pensions are already decreasing, since the introduction of the NPPS 2006;
> - the increases further compound the risk that members (particularly those young in service) will opt-out;
> - within the context of the public sector pay freeze and high inflation an increase to contribution rates is effectively a wage cut;
> - wanting to avoid a vicious circle of increasing contributions to cover opt-outs;
> - it could affect promotion;
> - the uncertainty surrounding police pay and conditions because of Tom Winsor's review; and
> - the unique employment status of police officers and the fact there is no recourse to arbitration on pensions' matters.
>
> I am aware that members of the fire fighters' pension schemes had their proposed contribution rate increases reduced – in some cases by half. The main reason given by the Department for Communities and Local Government (DCLG) was that "the altered levels of contributions will help reduce the risk of opt outs from the fire fighters' pension schemes."
>
> The fire fighters' pension schemes are similar to the police pension schemes and, like fire fighters (and the armed forces), police officers were recognised by Lord Hutton as requiring a lower normal pension age due to the unique nature of their work. Further, the DCLG said it would alter (ie, reduce) the pensions increase for fire fighters "in the

> light of the statutory consultation responses". Many of these responses were identical to reasons that Staff Side provided in its consultation response.[76]

On 19 April, the Home Secretary responded that contribution increases was only one element of the proposed reforms:

> [...] I have committed to taking a fair and even-handed approach to police officers on pension reform. I maintain that commitment. The increase in pension contributions is one element of proposed reforms and it is inevitable that there will be differences between schemes on individual elements. This is a consequence of meaningful discussions about how the reforms will be tailored to meet the varying requirements of different workforces. The Government has a clear intention to achieve the full savings from each scheme of a 3.2 percentage point average increase in contributions by 2014-15 for all relevant workforces.[...][77]

Judiciary

Until April 2012, judges only paid contributions towards survivors' benefits:

> 2. [...] The JPS are unfunded schemes and members do not currently pay contributions towards their own pension benefits. However, they do pay contributions towards the provision of a contingent pension for a surviving spouse, civil partner, or dependent children, known as widows/ers pension scheme or WPS.
>
> 3. In relation to the WPS, for those in schemes under the *Judicial Pensions Act 1981* the contribution rate is either 2.4% (although this now applies to very few judges) or 1.8% of gross salary depending on the particular scheme. Again in relation to the WPS, for those in the scheme under the *Judicial Pensions and Retirement Act 1993* scheme the contribution rate is 1.8% of pension capped salary.[78]

However, provisions in part 5 of the *Pensions Act 2011* provide for judges to contribute towards the cost of their personal benefits in future.[79] On 20 December, the Chief Secretary to the Treasury said reforms to pensions for the judiciary would be agreed "in due course."[80] In March 2012, Justice Secretary Kenneth Clarke announced "new net personal contributions of 1.28%" from April for members of the judicial pension schemes:

> **Judicial Pension Schemes**
>
> The Lord Chancellor and Secretary of State for Justice (Mr Kenneth Clarke): At the spending review 2010 the Government announced increases to member contribution rates in public service pension schemes saving £2.8 billion a year by 2014-15, to be phased in from April 2012.
>
> The *Judicial Pensions (Contributions) Regulations 2012*, laid today, will introduce from April new net personal contributions of 1.28% of salary for the members of the judicial pension schemes who have not accrued full pensions benefits. The regulations also set out when no contributions are due and ensure that the payment of personal judicial pensions contributions will have no impact on the maximum additional voluntary contributions that an individual may make.

[76] Letter to Home Secretary from PFEW, 10 April 2012
[77] Letter to General Secretary of PFEW from Home Secretary, 19 April 2012
[78] *Pensions Bill 2011 – Impacts – Annex E1*
[79] *Pensions Bill 2011 – Impacts – Annex E1*. The debate on this is covered in more detail in Library Research Paper RP 11/52 Pensions Bill
[80] HC Deb, 20 December 2011, c1206

> The Government remain committed to securing in full the spending review savings in 2013-14 and 2014-15 from further increases to member contributions to public service pension schemes.
>
> The associated *Judicial Pensions (European Court of Human Rights) (Amendment) Order 2012*, also laid today, will enable contributions towards the costs of providing personal benefits to be taken other than from salary, from the UK judge of the European Court of Human Rights if that judge continues to be a member of a judicial pensions scheme in line with the process already in place for collecting contributions towards dependants' benefits.[81]

MPs' pensions

On 17 October 2011, Members of Parliament agreed to a motion that responsibility for oversight of MPs' pensions should be transferred to the Independent Parliamentary Standards Authority (IPSA) and inviting IPSA to increase member contribution rates from 1 April 2012 in line with changes in pension contribution rates for other public service schemes:

> That this House reasserts its view that the salaries, pensions and expenses scheme for hon. Members ought to be determined independently of this House; accordingly invites the Leader of the House to make an order commencing those provisions of the *Constitutional Reform and Governance Act 2010* which transfer responsibility for the pensions of hon. Members to the Independent Parliamentary Standards Authority (IPSA); supports the approach to public service pension reform set out in the Final Report of the Independent Public Service Pensions Commission chaired by Lord Hutton of Furness; believes that IPSA should introduce, by 2015, a new pension scheme for hon. Members which is informed by the Commission's findings and their subsequent application to other public service pension schemes; recognises the case for an increase in pension contributions made in Lord Hutton's interim report; and accordingly invites IPSA to increase contribution rates for hon. Members from 1 April 2012 in line with changes in pension contribution rates for other public service schemes.[82]

The Order transferring responsibility for MPs' pensions to IPSA came into force on 24 October 2011.[83] On 8 February 2012, IPSA launched a public consultation on its recommendation to increase MPs' pension contributions by 1.85%.[84] It had considered whether the contribution increase should be delayed until a fundamental review of the scheme had been conducted but decided against:

> 18. One of IPSA's fundamental principles is that MPs should, as far as possible, be treated in the same manner as ordinary citizens. We have accordingly decided that it is fair that MPs, like the majority of other public sector workers, should pay more for their pensions this year. MPs at all levels of benefits will see an increase of contributions from 1 April. The changes will only apply to service from this date.[85]

Members can currently opt to make contributions at one of three rates, with pension benefits build up at different rates, depending on the contribution rate chosen:

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[81] HC Deb, 8 March 2012, c72-3
[82] HC Deb, 17 October 2011, c629
[83] *The Constitutional Reform and Governance Act 2010 (Commencement No. 6, Specified Day and Transitional Provision) Order 2011* (SI 2011/2485)
[84] MPs Pensions – Consultation – January 2012
[85] Ibid

- Members contributing at 11.9 per cent accrue pension benefits at a rate of 1/40th of salary for each year of service;
- Members contributing at 7.9 per cent have an accrual rate of 1/50th;
- Members contributing at 5.9 per cent have an accrual rate of 1/60th.

IPSA commented that the MPs' scheme was a "relatively high benefit scheme in comparison to most other public service schemes" and that the "high benefits made it expensive both to the taxpayer and to MPs." To mitigate the risk of MPs opting out of the scheme in response to the increased contribution rate, IPSA proposed giving them flexibility to "switch to a lower benefits tier for future pension accrual, dropping their contributions (and consequently their benefits) to a lower level".[86]

IPSA published its report on the consultation in March 2012. It concluded that member contributions should increase in April 2012:

> 9. As we set out in our consultation document, we consider it essential for public confidence in MPs, in Parliament and in the principles of independent regulation that MPs are not seen to be shielded from the increases applied to other public sector workers. We have also been influenced by the motion passed by the House of Commons, which invited us to increase contribution rates for MPs "In line with changes in pension contribution rates for other public service schemes".
>
> 10. We do not consider it appropriate to use only one scheme when deciding on a comparable increase. It is true that the local government scheme will not be applying an interim increase this year. But the members of that scheme are, by and large, paid significantly less than MPs and a lack of any immediate increase is unlikely to affect public confidence in the same way as it would for MPs. Instead, our proposals took account of the increases applied to a range of public service schemes and the fact that MPs already pay higher contributions as a proportion of income (and receive higher benefits) than many workers.
>
> 11. During the consultation process we considered applying different increases to the different levels of benefits. Such an approach might be fairer to the very small number of MPs who do not contribute at the top benefits level, but would introduce additional complexity to an already complex pension scheme. We also took account of the fact that previous increases in the MPs' Pension Scheme have applied a single increase across the benefits levels.
>
> 12. We have therefore decided that from 1 April 2012 there will be a 1.85% increase to all contribution rates. This will apply to future service only.[87]

Regarding the flexibility to switch to a different benefits level, it said it would give MPs "the option to move up as well as down" and that any change in benefits level should be levels to be backdated to 1 April 2012."

IPSA has now started on "root and branch review" of MPs' remuneration – pay and pensions. It plans to conduct a formal consultation is planned towards the end of 2012.[88]

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[86] IPSA, MPs' Pensions Report on the Consultation, March 2012
[87] Ibid
[88] IPSA, MPs' Pensions Report on the Consultation, March 2012

Ministerial Pensions

The Minister for the Cabinet Office has responsibility for Ministers' pensions.[89] Ministers' pensions are provided through the Ministerial section of the Parliamentary Contributory Pension Fund. Ministers who are MPs are eligible to be members of both the MP's and Ministerial sections. Contributions on their ministerial salary are paid at the same rate as those made under the MPs' section (see above). On 15 March 2012, Minister for the Cabinet Office, Francis Maude, announced increases in Ministerial contribution rates for 2012-13. In line with other public service schemes, a further consultation will take place on increases for 2013-14 and 2014-5:

> Last year, I consulted on proposals to make increases to member contributions in 2012-13 and this consultation concluded on 13 January. Having given careful consideration to the responses, I have decided to implement these proposals effective from 1 April 2012.
>
> This will mean that:
>
> - Secretaries of State, the Leader of the Opposition in the Commons and Speaker in the House of Lords will pay an additional 2.4 percentage points of pay;
>
> - Ministers of State, the Government Chief Whip, the Leader of the Opposition in the Lords, the Chairman of Committees of the House of Lords and the Deputy Chairman of Committees of the House of Lords will pay an additional 1.6 percentage points of pay; and
>
> - Parliamentary Under Secretaries, the Government Whips and Opposition Whips will pay an additional 1 percentage point of pay.
>
> In line with other public service schemes, a further consultation will take place on the contribution increases for members of the Ministerial Pension Scheme in 2013-14 and 2014-15. Before these increases are implemented, I will consider any evidence of opt-outs from the scheme in line with the Government's commitment given on 20 December by the Chief Secretary to the Treasury.
>
> The increased contributions will deliver an average of 1.7% percentage points of pay for the Ministerial Pension Scheme's membership. These additional contributions will mean that the increase in Exchequer contributions expected following the latest valuation of the Parliamentary Contributory Pension Fund will be lower than otherwise expected. Further, the Exchequer contribution will be reduced further to reflect increases in 2013-14 and 2014-15, following advice from the Government Actuary.
>
> Ministers in the House of Commons make separate contributions towards their pensions as MPs. Responsibility for the setting of pension provision for MPs is the responsibility of the Independent Parliamentary Standards Authority, which has consulted on proposals to increase MPs' contribution increases.[90]

4.3 Debate on the issues

This section attempts to summarise the main views put forward by the Government and trade unions. More detail can be found in Library standard notes covering individual schemes.[91]

[89] *The Constitutional Reform and Governance Act 2010 (Commencement No. 6, Specified Day and Transitional Provision) Order 2011* (SI 2011/2485)

[90] WMS, 15 March 2011

[91] There are links to this on page 1 of this note

The basis for reform

The Government argued that reforms to date have been insufficient to reverse the increase in costs of public service pensions from rising longevity and that employee contribution rates should increase so that they pay a higher proportion of the cost.

> The interim report of the Independent Public Service Pensions Commission, chaired by Lord Hutton, former Work and Pensions Secretary, sets out that there is a clear rationale for increasing employee contributions to public service pensions. The report found that the value of public service pensions has been increasing following a dramatic increase in life expectancy at retirement. Current pensioners are expected to spend over 40% of their adult lives in retirement, compared to 30% for pensioners in the 1950s. Members of all of the public service pension schemes have benefited from the increase in the value of their pension and most of these extra costs have fallen to employers and taxpayers. Increases in employee contributions will rebalance contributions, and ensure a fairer distribution of costs between members and other taxpayers.[92]

The trade unions disputed the argument that there is an imbalance between employer and employee contributions that justifies the proposed increases for employees. In its submission to the Commission's final report, the TUC argued that in practice, employees who contributed at relatively low rates saw this reflected in their pay levels:

> In terms of the respective shares of the cost of these schemes that is met by the employer and employees, there is no hard evidence of an imbalance, even when allowing for the increase in longevity that has occurred over the past 20 years. Both labour market theory and practical experience of trade union negotiators leave no doubt that pay levels are affected in practice both by the level of member contributions and the increasing cost to employers or providing pensions not only directly, in the form of member contributions but also indirectly, through an impact on the level of their pay. This adjustment is occasionally explicit, for example in the armed forces, but more typically it is implicit. Either way, the impact on members' pay ought not to be disregarded. [93]

Trade unions also argued that reforms introduced in 2007/08 – including "cap and share" (see section 3.2 above) - were designed to keep costs sustainable and that decisions on whether further reform is needed should be taken on the basis of scheme valuations. In its response to the consultation on increasing employee contributions in the teachers' scheme, for example, the NASUWT said:

> 4. The NASUWT accepts that, in principle and in practice, contribution rates may vary over time as the viability of the Teachers' Pension Scheme (TPS) necessitates. The NASUWT continues to endorse the operation of the 'cap and share' arrangements agreed for reform of the pension scheme in 2006, which were designed specifically to ensure the future viability and sustainability of the TPS in the long term.
>
> 5. The proposal to impose increased contributions on teachers is not only premature, it is also wholly unjustified. The DfE and the Treasury have flatly refused to commission the valuation of the TPS, which is necessary for the purposes of determining changes to contributions within the TPS. There is, therefore, no objective data on which to base any decisions about increasing contributions – both in terms of justifying the quantum

[92] HC Deb, 1 Mar 2011, c 438W; See also, HM Treasury, Public Service Pensions: good pensions that last, Cm 6214, November 2011, para 1.9, and Danny Alexander, Speech to IPPR, 17 June 2011; David Cameron, Speech to the Local Government Association, Tuesday 28 June 2011

[93] TUC evidence to the Independent Public Service Pensions Commission no. 2, December 2010

of any such increases or in relation to determining the basis for distributing the relative burden of increased contributions onto employees.

6. The NASUWT rejects therefore what is in effect a pensions tax on teachers and rejects entirely any suggestion that there can be meaningful consultation on the implementation of the proposal for increasing employee contributions in the absence of up-to-date and objective data on the operation, performance and sustainability of the TPS.[94]

The FDA said:

The money to be raised from increased pension contributions is effectively a levy on public sector workers as part of the Government's deficit reduction plans. The increased contributions have not been determined following any assessment of the costs of providing pensions for FDA members, and the finance raised will not be used for that purpose.

[...]

All public sector unions agreed changes to pension schemes in 2007, which provided long-term sustainability. This would have involved scheme valuations in 2010 to determine whether there were any increased costs. These arrangements have been abandoned following the Government's refusal to allow scheme valuations to proceed. This shows that the increase in contributions is not about the costs of the pension scheme, it is an additional tax on public sector workers going straight to the Treasury.[95]

However, the Government rejected this approach, arguing that cap and share is an untried system and would not address significant cost increases from past improvements in life-expectancy:

[...] Cap and share was designed to prevent further increases in costs to taxpayers. But it did not address the already significant cost increases from past improvements in life expectancy. Nor did it specify how these savings would be made. It left public service workers without certainty about the contributions they would pay or the benefits they would receive in future.[96]

Instead, it decided to achieve the savings expected from cap and share in 2012/13 through contribution increases:

Because of previously agreed 'cap and share' arrangements contribution increases in some schemes were anticipated to be required in 2012. To meet the 2012-13 savings target from increased contributions announced in the Spending Review a formal consultation will shortly commence on each schemes' proposals for increases from April 2012, to secure savings of £1.2 bn in that year across the unfunded schemes. These consultations will be completed by the end of October, in order to ensure

[94] NASUWT, Consultation response. Department for Education Consultation on Proposed Increases to Contributions for Members of the Teachers' Pension Scheme. October 2011; NUT press release, NUT to strike on 30 June 2011, 15 June 2011; ATL Pensions Update, April 2011

[95] FDA, Principal Civil Service Pension Scheme. Consultation on Proposed Increases to Employee Contribution Rates Effective from April 2012, FDA response

[96] HM Treasury, Public Service Pensions: good pensions that last, Cm 6214, November 2011, para 1.5-7

implementation by April 2012. This will replace 'cap and share', which will be suspended.[97]

Consultation process

Trade unions were also concerned at the limited scope of the consultation. The FDA said:

> 3. The main points the FDA would like to make on the consultation exercise are as follows:
>
> (i) The scope of the consultation is so narrow as to be almost meaningless. The consultation does not seek views about the overall amount to be raised, or when. Nor does it consider alternative means of raising the amount specified; instead, the consultation is merely about the distribution of the pain of pension contribution increases;
>
> (ii) An increase in contributions is a significant further reduction in take home pay and thus living standards. During a pay freeze, with high inflation rates, it is particularly damaging and resented by our members;
>
> (iii) Pensions are part of the total remuneration package and any proposal to increase pension contributions must form part of a wider consideration of total reward;
>
> (iv) The current proposals are not about securing long-term sustainability of public sector pensions. The increased contributions proposed have not been determined following any assessment of the costs of providing pensions for FDA members, and the finance raised will not be used for that purpose. Instead, the contribution increase is nothing more than a levy on civil servants as part of the deficit reduction programme;
>
> (v) There is significant evidence to show that the costs of public sector pensions are falling;
>
> (vi) The proposals must be subject to a full equality impact assessment;
>
> (vii) There is a high risk that, if implemented, these proposals will lead to an increasing number of scheme members opting out;
>
> (viii) All the key issues – employee contribution increases, the Hutton recommendations, the impact on total reward and the move from RPI to CPI - should be considered together to try and find an acceptable package of reform; and
>
> (ix) The FDA is opposed to the imposition, without agreement, of any increases to employee pension contributions.[98]

The Fire Brigades Union said:

> 50, Furthermore, the proposed 3.0% imposition to employer contributions across pension schemes has not taken into consideration the fact that FPS and NFPS contribution rates are amongst the highest in the public sector. The differences between the employee contribution rates in the schemes, and the reasons for them, were not examined in the Spending Review and will leave firefighters in a no-win situation. They will not be able to afford the new contribution rates, but opting out and therefore becoming a deferred member when they have made considerable contributions is unpalatable. If the Commission is to be seen to be ensuring that

[97] HC Deb, 19 July 2011, c91-4; Letter from the Chief Secretary to the Treasury to TUC General Secretary, Brendan Barber, 18 July 2011

[98] FDA, Principal Civil service Pension Scheme – Consultation on Proposed Increases to Employee Contribution Rates Effective from April 2012, FDA Response

firefighter pensions remain sustainable, affordable and fair it must recognize that it also must be sustainable, affordable and fair to the employee who is contributing and these new imposed contribution rates do not satisfy that test.[99]

Impact on members

Trade unions are also concerned at the impact contributions, particularly at a time of pay restraint. The Royal College of Nursing, for example, said:

> RCN members find themselves in the middle of a two year pay freeze with NHS employers seeking to further cut their earnings by making changes to the national agreed pay system, Agenda for Change. In September CPI was 5.2% and RPI was 5.6% while public sector (excluding financial services) average earnings growth (total pay) in 3 months to August was 1.7% and 3% in the private sector.[100]

Some unions, based on surveys of their members, have raised concerns that the increase might lead to large numbers opting out of the schemes. For example, UNISON said a survey of its healthcare members showed that:

> – 57% of respondees said they cannot afford 2012-2013 proposed member contribution increases
>
> – 21% of respondees said they would opt-out of the scheme if proposed 2012-2013 member contribution increases are implemented
>
> – 75% of respondees said they won't be able to afford contribution increases for 2013 and 2014 if these follow the same split as proposed contribution increases for 2012-2013
>
> – 37% of respondees said they would opt-out of the scheme if likely member contribution increases for 2013 and 2014 took effect[101]

The Government argues that despite contribution increases public service pensions remain an "excellent investment for retirement."[102] It has assumed "an increase in the opt-out rate equal to one per cent of total paybill" in consequence of the proposed contribution.[103] In addition, it says the increases will be implemented in a way to mitigate the risk of opt outs (phased-in and with protection for the low-paid) and that it will review the impact of the 2012/13 increases before taking final decisions on how future increases will be delivered.[104]

Part-time workers

Trade unions and others have raised particular concerns about the impact on low-paid part-time workers, who will see their contributions increase because their salary on a full-time equivalent (FTE) basis exceeds £15,000. The Local Government Group suggests not:

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[99] Evidence from the Fire Bridgades Union to the Independent Public Service Pensions Commission's call for further evidence, December 2010

[100] DoH, NHS Pension Scheme. Consultation on proposed increase to employee contribution rates effective from April 2012, Government response, 8 December 2012; See also FDA, Increased pension contributions: no justification, 2011

[101] UNISON response to Department of Health NHS Pension Scheme Consultation on proposed increases to employee contribution rates effective from April 2012, October 2012; See also, FBU briefing, Pensions No 1, 8 July 2011

[102] DoH, NHS Pension Scheme. Consultation on proposed increase to employee contribution rates effective from April 2012, Government response, 8 December 2012

[103] HM Treasury, Spending Review – policy costings, October 2010

[104] HM Treasury press release, Government announces Heads of Agreement on public service pension reform, 20 December 2011

> Part-time employees, who constitute the overwhelming majority of low paid workers in local government, have their contribution rate assessed by reference to their wholetime equivalent salary. Thus, many of those part-time employees with part-time salaries below the low pay protection threshold will, in fact, not benefit from the protection (because their whole time equivalent salary is greater than £24,000).[105]

Unions have also commented on this. For example, the FDA said:

> 36. FDA members who work part-time will pay the percentage increase in contributions relevant to the full-time equivalent salary level. In some cases this will result in FDA members paying the same percentage increase as those earning significantly more but, crucially, they will not benefit from the higher rate of tax relief applicable at that salary level.[106]

Around 1 in 5 civil servants work part-time (85% of them women).[107]

The Government says the rationale for basing the contribution rate on full-time equivalent (FTE) salary is that it is this which is used to calculate pension entitlement and it would be unfair to full-time staff to treat part-time staff differently.[108] This was explained in more detail in the Government's response to the consultation on increases for NHS staff:

> 4.35 For example, a member who works full-time earning £15,000 would pay a contribution of 5% (gross) whereas a part-time worker earning £15,000 in a role that has a full-time equivalent salary of £30,000 would contribute 8% (gross) under the revised proposal described in section 5.
>
> 4.36 The percentage contribution rate is set according to the full-time equivalent pay of part-time staff. However a part-time worker would then pay contributions equal to that percentage contribution rate of their actual part-time pay. The part-time worker's length of service would also be scaled down to its full-time equivalent length.
>
> 4.37 This approach was agreed with the NHS Trade Unions as the best way forward when tiered contribution rates were introduced.
>
> 4.38 To illustrate, if we compare the pensions of two nurses who are doing the same role – one working full-time earning £30,000, and one whose full-time equivalent pay is £30,000 but who is working part-time at half of full-time hours and earning £15,000 –
>
> > The full-time nurse pays 8% contributions (£2,400) on £30,000 and earns 1/80th of this as pension - worth £375 per annum
> >
> > The part-time nurse pays 8% contribution (1,200) on £15,000 which is half of £30,000 and earns half of 1/80th of this as pension - worth £187.50 per annum
>
> 4.39 £187.50 is half of £375. Therefore this is fair and equitable as the part-timer is working half the hours of the full timer, is earning half the pay of the full timer, is paying

[105] Letter to Chancellor from Local Government Group 16 February 2011

[106] FDA, Response to the proposed increase in pension contributions in April 2012; See also the response from the trade union, UNISON

[107] Cabinet Office, Principal Civil Service Pension Scheme – Consultation on proposed increases to employee contribution rates effective from April 2012, 28 July 2011

[108] DfE, Consultation on Proposed Increases to Contributions for Members of the Teachers' Pension Scheme, 28 July 2011

pension contributions that are half those of the full timer and is getting a pension that is half that of the full timer.[109]

[109] DoH, NHS Pension Scheme. Consultation on proposed increase to employee contribution rates effective from April 2012, Government response, 8 December 2012